No. 14112

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

LOIS J. NEWMAN (formerly Lois J. Senderman),

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S OPENING BRIEF.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

Statutes

Textbooks

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Nature of the Controversy.

The controversy involves the determination of the year in which petitioner made a gift. The petitioner made a gift in trust to her daughter in 1943. She filed Federal and State gift tax returns. The value of the gift was reported in the Federal return as $30,000.00 with no gift tax payable thereon. The petitioner asserts that a completed gift occurred in 1943.

Respondent asserts that the completed gift occurred in 1946 when the same property was valued at $151,051.09. The gift in 1943 was made to a trustee who died in 1946. Upon his death in 1946, the corpus of the trust was distributed to the duly appointed guardian of the beneficiary and by reason thereof, respondent asserts that the com-

pleted gift occurred in 1946. This assertion is made, although there is nothing in the record to establish any act by petitioner in 1946 to make or complete a gift; nor is there anything shown to establish that in 1946 the petitioner could have prevented distribution of the trust to the guardian of the beneficiary.

The Tax Court determined a gift tax deficiency of $50,079.84 for 1946. Awaiting the determination of this appeal is a controversy involving a proposed overassessment of income taxes in the sum of $62,763.47 paid to the minor and the minor's trust in 1943, 1944 and 1945, and income tax deficiencies against petitioner in the sum of $244,384.39 for the years 1943 to 1947, inclusive. Said deficiencies are based mainly, and said overassessments are based wholly, upon including in petitioner's income all of the income reported by said trust and by said minor during said calendar years. [R. 32-34.]

There seems to be no question that petitioner intended to create an oral irrevocable trust in 1943. Subsequently, the trustee, her attorney, prepared and executed a written instrument acknowledging that he was holding the trust estate, but he failed to use the magic word "irrevocable" and by reason of this failure, respondent claims petitioner must now pay almost $300,000.00 in taxes for making a $30,000.00 gift in 1943.

Pleadings and Jurisdictional Facts.

On July 24, 1950, the above-named petitioner filed her Petition in the Tax Court of the United States for redetermination of a deficiency for gift taxes for the calendar year 1946 in the amount of $71,195.99. Petitioner alleged that she established an irrevocable oral trust for the benefit of her daughter in 1943 and the Commissioner

erred in determining that petitioner made a gift or gifts during the calendar year 1946. [R. 5-14.]

An Answer was filed in the Tax Court on September 19, 1950. [R. 15-17.] Thereafter, an Amended Petition [R. 17-23] and Answer to Amended Petition [R. 23-25] were filed.

A Stipulation of Facts was filed in the Tax Court on November 2, 1951 [R. 26-92], on which day the hearing was held before the Tax Court sitting in San Francisco, California. [R. 115-190.]

Following the promulgation of Findings of Fact and Opinion [R. 93-111], the Tax Court entered its Decision on May 15, 1953, that there is a deficiency of $50,079.84 in gift tax for the year 1946. [R. 111-112.]

Petition for Review by this Court of said Decision was filed August 10, 1953. [R. 112-114.] Said Petition was docketed on November 2, 1953 [R. 191], and the Statement of Points [R. 192-193] and Designation of Contents of Record on Review [R. 193-194] were filed December 2, 1953.

This Court has jurisdiction pursuant to Section 1141(a) of the Internal Revenue Code. (26 U. S. Code, Sec. 1141(a).)

Statement of the Case.

Petitioner has a daughter named Lois E. Senderman, born May 14, 1935. Said daughter was the issue of petitioner's marriage to Aaron Senderman, which marriage ended by divorce in 1940. At all times material hereto prior to December, 1944, petitioner's name was Lois J. Senderman; in December, 1944, she married Louis Newman and since then her name has been Lois J. Newman. [R. 26.]

The Oral Trust.

Prior to January 1, 1943, petitioner owned 2396⅞ shares of stock of Aztec Brewing Company, a California corporation, which stock she had acquired by inheritance from her parents. [R. 26, 129.] On or about January 1, 1943, petitioner conveyed 800 shares of said stock to her attorney, Richard S. Goldman, as trustee, to be held by him for her daughter, Lois E. Senderman. [R. 27, 125-128, 158-160.]

The record contains the uncontradicted testimony of petitioner and Clarissa Shortall, an attorney who was associated with Mr. Goldman, that on or about January 1, 1943, petitioner created an *oral irrevocable trust* of said 800 shares; Mr. Goldman being the trustee and petitioner's daughter the beneficiary. [R. 125-128, 158-160.] Respondent has stipulated that Mr. Goldman became trustee of said 800 shares in trust for petitioner's daughter in 1943, but contends that the trust was revocable and therefore the gift was not completed until 1946.

We submit that all of the facts clearly indicate that an oral irrevocable trust was created in 1943.

Petitioner testified that in several periods of her life she had "quite a bit of money" which she dissipated; that when her father was alive she "leaned very heavily" upon him; when her father died he left debts and the stock of the Aztec Brewing Company which was practically worthless at the time of his death. [R. 125.] She had been married to a man who was financially irresponsible and she and her former husband had dissipated a great deal of money. [R. 126.]

As the stock increased in value, petitioner realized that with the death of her parents that "this was the last

money" she might have and she wanted to provide for her daughter. She spoke to Mr. Goldman about this wish to provide for her daughter. [R. 126.]

They discussed 800 shares as they thought it would be valued at $30,000.00. [R. 126.] The mere fact of the mention of the specific exemption amount of $30,000.00 is clear evidence petitioner and her attorney were talking about making a completed gift in 1943 which would not incur any gift tax liability. Petitioner testified in a frank manner as to this gift, the reasons for the gift and the amount.[1]

Mr. Goldman told her that once she created the trust, no matter what she did or what happened to her, the money would be out of her reach forever.[2] With this admonition, petitioner was still willing to provide for her daughter but Mr. Goldman wanted her to think it over.

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[1]Petitioner testified:

"At the time I had this stock, but actually very little money, and we came to the conclusion that I could give her about 800 shares of the brewery stock—the value was about $30,000—and that I would incur no cash outlay or no further responsibility—I mean to pay any more money.

"I did this because I wanted to feel that if I was foolish, or remarried, that the child would be provided for. I wanted to see that she would attain maturity and have enough to be educated and have a little money to go on. I didn't think at that time—I don't think anybody did—that the stock would become as valuable as it did. I don't think anybody foresaw that. If I had known that I wouldn't have been so anxious to provide for her future, but I wanted to see that she did have something." [R. 126-127.]

[2]"He continued to impress upon me the fact: 'Remember, once this is done, no matter what happens, no matter if you need the money or not, you will not be able to touch this money.'

"I told him yes, I wanted the trust made.

"He said, 'I want you to think about it. Think it over very carefully.'" [R. 127.]

In January, 1943, petitioner told Mr. Goldman she thought it over and "wanted the trust made for her daughter." She told him: "I didn't want anybody able to touch the child's money, myself included—particularly myself, I guess." [R. 128.]

Mr. Goldman said the "trust stands of today. From today on I will be the trustee." [R. 128.] Mr. Goldman told her he was busy then but he would have the documents drawn up.

Petitioner's testimony was corroborated by Clarissa Shortall, a member of the State Bar of California since 1935. [R. 158-160.][3] Yet the Tax Court chose to ignore this oral irrevocable trust by reason of Mr. Goldman's preparation and execution of a written instrument which we shall next discuss.

The Opinion of the Tax Court recognized that both Mr. Goldman and Miss Shortall understood that petitioner wanted an irrevocable trust, *but solely because the subsequent written instrument did not use the word "irrevocable" the Tax Court held there was no completed gift in 1943.*

Laymen have long accused the legal profession of twisting true intents and cleverly using a word or two to accomplish a result not intended and inequitable. Most lawyers quickly assure their clients and lay friends that there are no mysterious devices or secret "hocus pocus" tricks used by the legal profession, but it is just that we have rules of law governing our conduct and affairs, which rules are logically and equitably administered to accomplish justice. We submit that it would take great

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[3]Miss Shortall was associated with Mr. Goldman in 1943.

persuasion to convince laymen (and lawyers) that our laws are fair and enforced justly and equitably should they learn that a lawyer's failure to insert one word in a document, *the lawyer prepared and signed,* cost his client over one-quarter of a million dollars.[4]

The Written Instrument.

Some months after the creation of said oral irrevocable trust, Mr. Goldman prepared and executed a written instrument which was pre-dated to January 1, 1943. [Stipulation of Facts, Ex. 2-B; R. 38-41.]

Miss Shortall testified that Mr. Goldman was a busy lawyer (probably overworked as most lawyers) and a man who had been in practice in San Francisco since about 1913. [R. 161-162.] In 1946, Mr. Goldman committed suicide. [R. 28, 125.] Under such circumstances we hesitate to comment unfavorably as to a deceased lawyer's draftsmanship, but we submit that this instrument which respondent contends made an oral irrevocable trust revocable is not a model of drafstmanship. The written instrument does not contain any declaration of

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[4]The Commissioner's position is that a completed gift was not made until 1946, when the interest in the Aztec Brewery Company had increased from $30,000.00 in 1943 to $151,051.09 in 1946, resulting in the deficiency gift tax of $50,079.84. However, the Commissioner asserts in a proceeding in the Tax Court still pending that if the gift was not completed until 1946, the income tax paid on behalf of the minor is to be returned and, accordingly, has determined deficiencies in petitioner's income taxes in excess of $200,000.00. The Commissioner determined a further gift tax deficiency based on the contention that the proposed overassessment of income taxes to the trust was a further gift by petitioner. The Tax Court held that since the income tax liability question is not settled, "we have no alternative to holding as error, the inclusion of the controverted and contingent amount within the gift consummated May 2, 1946." [R. 111; also see R. 32-34, 99-101, 109-111.]

trust by a trustor; in fact, it was more of a deposit receipt by Mr. Goldman for certain property held by him for petitioner *and for petitioner's minor daughter.*

In said written instrument, Richard S. Goldman acknowledged that he had in his possession 3 certificates of the capital stock of Aztec Brewing Company, certificate No. 12 for 2394⅞ shares standing in the name of Richard S. Goldman, trustee for Lois Senderman, certificate No. 13 for 1 share standing in the name of Phillip Storer Thacher and certificate No. 18 for 1 share standing in the name of Lois J. Senderman; that he held all of the certificates as Trustee and that the beneficial owners of the stock were Lois J. Senderman, owner of 1596⅞ shares, and Lois E. Senderman, a minor, the daughter of Lois J. Senderman, owner of 800 shares. The document further went on to set forth certain agreements by the Trustee with reference to the 800 shares and any other property which the *said minor daughter might thereafter deposit with him.* He agreed in subdivision (2) that he would deliver the property to any duly appointed guardian of the minor; if no guardian was appointed, to deliver the property to the child upon her attaining the age of 21 years. Amongst other agreements in subdivision 3 the Trustee provided for his resignation, discharge or death, in which event the property was to be transferred into the name of the duly appointed guardian of said minor. This document was in the form of a recital of facts by "The undersigned, Richard S. Goldman." [R. 38.]

Although this document doesn't contain the word "irrevocable," it should be kept in mind that it was not a formal declaration of trust by petitioner. Moreover, the written instrument clearly treats the 800 shares as a

completed gift and the property of the minor, Lois E. Senderman.

We think it important to stress that Mr. Goldman agreed to hold the 800 shares of stock "and any other property, real or personal, *which said Lois E. Senderman* (the minor) *may hereafter deposit with him.*" [R. 38; emphasis supplied.] Petitioner did not sign as "Trustor." Petitioner signed the instrument "individually" and as "Mother and Guardian of Lois E. Senderman, a minor." Her signature was under a separate paragraph below Mr. Goldman's signature and in which paragraph she acknowledged receipt of a copy of the instrument and she agreed that she and her daughter would be bound thereby.

The Gift Tax Returns.

Petitioner filed Federal and State of California gift tax returns for the calendar year 1943 in which she reported a gift to her daughter of said 800 shares of stock. [R. 27, 35.] The value of the gift was reported in the Federal return as $30,000.00, with no gift tax payable thereon. [R. 35.]

The $30,000.00 valuation was also placed upon the 800 shares in the State of California gift tax return. The State of California inquired as to the facts on which said valuation was based and determined a deficiency in petitioner's 1943 State of California gift tax, which deficiency was paid by petitioner. [R. 27-28.]

The Probate Court Proceedings.

On April 5, 1946, in a proceeding designated "In the Matter of the Irrevocable Trust of Lois E. Senderman, Beneficiary, and Lois J. Senderman, Donor and Trustor, and Richard S. Goldman, Trustee," a petition was filed by

the executor of the Estate of Richard S. Goldman with the Superior Court of the State of California in and for the City and County of San Francisco (hereinafter referred to as the Probate Court) for the appointment of a successor trustee or trustees in place of the deceased trustee. [R. 28-29, 56-59.]

On April 5, 1946, the Probate Court issued its order appointing Clarissa Shortall as successor trustee in place of the deceased trustee. [R. 29, 60.]

On May 2, 1946, a petition was filed in the Probate Court by the executor of the estate of said Richard S. Goldman for the appointment of a guardian of the Estate of said Lois E. Senderman. [R. 29, 61-65.]

On May 2, 1946, the Probate Court issued its order appointing Clarissa Shortall as guardian of the Estate of said Lois E. Senderman. [R. 29, 65-73.] It is this order by the Probate Court whereby the assets held for the minor were transferred to the minor's duly appointed guardian which respondent contends created the taxable event in 1946.

In April and in June, 1947, the said guardian filed a petition and amended petition, respectively, for instructions.[5] [R. 29-30, 74-82.] Notice of the hearing was duly given to the petitioner herein; to the minor's father,

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[5]Respondent and the Tax Court attach great importance to the fact that the Petition for Instructions was not filed until after the revenue agent raised the question of revocability and possible tax consequences. [R. 107.] Miss Shortall testified that when the revenue agent raised the question of revocability, she was afraid that Mrs. Newman might be glad to accede to that position and try to get the property back and the petition was filed to protect the minor's assets. She pointed out that although Mrs. Newman received $320,000.00 in distribution of Aztec Brewery profits from May, 1946, to June, 1947, she had requested an allowance from the guardianship estate to support her daughter on the

Aaron Senderman; to the Commissioner of Internal Revenue, Washington, D. C.; to the Secretary of the Treasury, Washington, D. C.; to the Internal Revenue Agent in Charge, San Francisco, California; and to the Collector of Internal Revenue, San Francisco, California. The petitioner and the guardian appeared in person, each with an attorney. Oral and documentary evidence was introduced and the issue was argued by counsel. The Court, having considered the evidence and arguments, found that Lois J. Newman created an irrevocable oral trust of 800 shares of stock. The Court further found that 6 or 7 months later the trustee executed a written declaration of trust which, while it failed to expressly state that it was irrevocable, did not terminate the oral trust but said oral trust continued in full force and effect until terminated. [R. 83-88.]

Specification of Errors.

Petitioner assigns as error the following acts and omissions of the Tax Court of the United States:

(1) The ruling that the completed gift did not occur in 1943 is contrary to the evidence.

(2) The ruling that the completed gift occurred in 1946 is contrary to the evidence.

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ground that she was not financially able to take care of her daughter. [R. 171-172.]

Miss Shortall testified:

> "For that reason, and because of other knowledge that I had, I realized that Mrs. Newman was spending a great deal of money. I knew that Mrs. Newman gambled. And I was rather concerned that she might find herself in a position where, because of the suggestion that was put in her mind by the Internal Revenue Agent that the trust could be revoked, she might be tempted to revoke the trust, and get some of the money back." [R. 172.]

(3) With no conflicting evidence, finding facts contrary to the evidence presented.

(4) Disregarding the order of the Superior Court in and for the County of San Francisco, California.

(5) Failing to recognize the substance, rather than the form, of a transaction.

(6) The finding of deficiency of gift tax for the year 1946.

(7) Failing to find taxpayer on January 1, 1943, declared Richard S. Goldman Trustee of irrevocable trust.

(8) Failing to find that taxpayer had no donative intent in 1946.

(9) Holding that the trust became irrevocable upon appointment of guardian.

Summary of the Argument.

1. The valid decree of the California Probate Code construing the oral trust as irrevocable was binding upon the Tax Court.

2. Petitioner could not have prevented the distribution to the guardian on May 2, 1946, or the making of the Order holding the oral trust irrevocable.

3. Petitioner made a completed oral gift in 1943.

4. It was error for the Tax Court to disregard the oral irrevocable trust and determine the controversy on the basis of the written instrument.

5. The written instrument did not create a revocable trust.

6. The transfer of the assets to the guardian in 1946 did not constitute a taxable gift.

ARGUMENT.

I.

The Valid Decree of the California Probate Court Construing the Oral Trust as Irrevocable Was Binding Upon the Tax Court.

California law determines whether the trust is revocable or irrevocable. (*Freuler v. Helvering,* 291 U. S. 35, 54 S. Ct. 308 (1934).) The Tax Court is bound to follow California law.

The best authority on the California law applicable to the controversy presented herein is the California Probate Court Order which held that the oral trust was irrevocable. [R. 83-88.]

In 1947, the California Probate Court had before it the direct issue as to whether or not an oral irrevocable trust was created in 1943. The Court held that an oral irrevocable trust was created in 1943; the Court further stated in its Order that the Court fully considered the evidence and the arguments of the parties.

The Tax Court refused to follow the California court's decision, stating as its reason:

> "There was no controversy between the parties and no independent judgment was rendered." [R. 104.]

This statement of the rule of recognition is erroneous as will be demonstrated herein.[6]

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[6]Notwithstanding the fact that the Judge of the Probate Court signed his name to an Order which recited that it was made upon full consideration of the evidence and the arguments of adverse counsel, the Tax Court treats the Order as "merely a consent decree entered *pro forma* in a friendly suit." [R. 104.] With due respect to the Tax Court, as members of the State Bar of California we respectfully submit that there is nothing in the record which justified a comment that the California Probate Court acts in a *"pro forma"* manner with respect to any matters, in particular, with respect to proceedings involving the estates of minors.

The Order showed that notice of the hearing was duly given to all parties, including the respondent herein, the Secretary of the Treasury, the Collector of Internal Revenue and Internal Revenue Agent in charge in San Francisco. [R. 83-84.] Despite the fact that respondent had notice of the hearing, the Government failed to appear but elected to wait until the matter got to the Tax Court and then take the position that the California Probate Court proceedings are a nullity. Both the guardian of the minor and the petitioner herein appeared in person and each was represented by counsel. Evidence both oral and documentary was offered and introduced by the respective parties. The issues were argued by counsel and the Court decided that an oral irrevocable trust was created after considering the evidence and the arguments according to its own Order. [R. 83, 98.]

The decision of the California Probate Court has not been reversed or overruled. Respondent has been unable to point to any decision or statute which would indicate that it is erroneous. It is not questioned that under California law the decision is binding upon the guardian and the petitioner.

The Order of the California Court was that ". . . Lois J. Senderman (now Lois J. Newman) orally created an irrevocable trust. . . ." [R. 87.] That decree adjudicated and determined the conflicting interests of the parties before the Court. The decision by the Court having jurisdiction of the parties and the property stands as the final and ultimate determination of the property rights of the parties.

It is clear in the proceedings before the California court that petitioner's interest as settlor of the trust was absolutely adverse to that of the guardian. At that time the

assets held for the minor were considerable in relation to the petitioner's own personal assets.[7] If Mrs. Newman were able to establish that the trust was revocable, she would have received over $300,000.00[8]

Where the claims of the parties are adverse and are determined without fraud and collusion, Probate Court decrees determining such claims are to be given binding effect. That this is the applicable rule of law is recognized by the Court of Appeals for the Sixth Circuit in a decision handed down five days after the Tax Court opinion in this cause was promulgated.

Goodwin's Estate v. Commissioner of Internal Revenue, 201 F. 2d 576 (6th Cir., 1953).

The principal issue in the *Goodwin* case was the binding effect for tax purposes of a decree of a Probate Court. The executrix of the estate (widow of the deceased) filed a motion with the Probate Court requesting approval of claims made against the estate by her daughters. At the hearing on the motion, *ex parte* evidence was received from two of the claimants and oral testimony from another. The Court allowed the claims. The Commissioner of Internal Revenue determined that the claims were not lawful deductions, that the Probate Court decree should be ignored and asserted a deficiency claim. This position

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[7]The value of the trust *res* in 1946 was determined to be "not over $228,831.49" plus $88,529.10, or a *total* of $317,360.59. [R. 21.]

[8]The record is clear that petitioner was a person who dissipated her assets with ease and regularity and, accordingly, had constant need of money. She testified that if she had known the interest in the Aztec Brewery would become as valuable as it did, she "wouldn't have been so anxious to provide for her (the daughter's) future . . ." [R. 127.] There is no reason to believe that in 1946 petitioner didn't want the property back; but she didn't stand a chance of getting it back unless she perjured herself.

was sustained by the Tax Court. The Court of Appeals overruled the Tax Court and recognized the binding effect of the Probate Court decree.[9]

The Court of Appeals expressly rejected the Commissioner's contention that the decree of the Probate Court should not be recognized because there was no contest.

> "Clearly the Probate Court proceeding was not an active and genuine contest for every party to the proceeding agreed that the claims were valid. However, the petitioner was a party having an interest adverse to the interests of the daughters. As widow of the decedent, petitioner was entitled to one-third of the net estate administered in the Probate Court after payment of claims against the estate. * * * It is undisputed that he payment of the claims of the daughters reduced the distributive share of the widow over $30,000. * * *

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[9]It is significant to note that Treasury Regulation 105, §81.30, which the Court of Appeals cited provide that contested proceedings are not a *sine qua non* to recognition of a State court decrees with respect to claims against an estate. A portion of the Regulations quoted by the Court of Appeals reads as follows:

> "Regulation 105, §81.30. *Effect of court decree.* The decision of a local court as to the amount of a claim or administration expense would ordinarily be accepted if the court passes upon the facts upon which deductibility depends. * * * For example, if the question before the court is whether a claim should be allowed the decree allowing it will ordinarily be accepted as establishing the validity and amount of the claim. The decree will not necessarily be accepted even though it purports to decide the facts upon which deductibility depends. It must appear that the court actually passed upon the merits of the case. This will be presumed in all cases of an active and genuine contest. * * * If the decree was rendered by consent, it will be accepted, providing the consent was a bona fide recognition of the validity of the claim—not a mere cloak for a gift—and was accepted by the court as satisfactory evidence upon the merits. *It will be presumed that the consent was of this character and was so accepted if given by all parties having an interest adverse to the claimant* * * *." (*Id.*, 201 F. 2d at pp. 579-580; emphasis supplied.)

"The decree of the Probate Court was rendered after a hearing of which all parties had notice and in which oral testimony was taken. While consent to the entry of the decree was given, it was given 'by all parties having an interest adverse to the claimant.' * * *." (*Id.,* 201 F. 2d at p. 580.)

The Court of Appeals in the *Goodwin* case discussed the origin of the recognition doctrine:

"As to other provisions, the (Treasury) Regulations follow and amplify in practical detail the long existing case law upon this question. In *Freuler v. Helvering,* 291 U. S. 35, 54 S. Ct. 308, 312, 78 L. Ed. 634, it was held that the decree of a state court establishing the rights of beneficiaries under a trust must be considered in applying the Revenue Act of 1921. The court said, 'The rights of the beneficiaries are property rights and the court has adjudicated them.' This was followed by *Blair v. Commissioner,* 300 U. S. 5, 57 S. Ct. 330, 81 L. Ed. 465, opinion by Chief Justice Hughes. * * *

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"Respondent also contends in effect that the Regulations do not apply because the order of the Probate Court was not a decision on the merits. Here the Probate Court in a formal motion was requested to rule upon the validity of the claims involved. Notice was duly given, a public hearing was held, and oral testimony was taken. The Probate Court had exclusive jurisdiction of the subject matter. (Citing authorities.) It was empowered to determine all questions of fact underlying its decisions. (Citing authority.) While an appeal from the order of the Probate Court could have been taken to the Court of Common Pleas, no appeal proceedings were instituted. The Probate Court's decision by its allowance of the claims substantially and adversely

affected the property rights of three beneficiaries of the estate. This was undeniably a decision on the merits and the Regulations were squarely applicable." (*Id.*, 201 F. 2d at pp. 580-581.)

In *Henricksen v. Baker-Boyer National Bank,* 139 F. 2d 877 (9th Cir., 1944), the Commissioner sought to disallow as deductions in the estate tax return bequests for charitable purposes because of the alleged right of the widow to invade the corpus of the estate. Prior to filing of the estate tax return, the executor of the estate and trustee petitioned the Superior Court in Washington for a construction of the terms of the will and the Superior Court ruled that pursuant to the will, the widow did not have the power to invade the corpus.

In the *Henricksen* case the Commissioner argued that the Order of the Superior Court was not entitled to recognition as it was rendered in a non-adversary proceeding; the Commissioner also argued that neither the widow nor the remainder interests were parties to the proceeding. This Court held that the Order of the Superior Court was conclusive of the issue. (*Id.*, 139 F. 2d at p. 882.)[10]

Also see *Letts v. Commissioner of Internal Revenue,* 84 F. 2d 760 (9th Cir., 1936), where this Court held that the Commissioner was bound by a state court order approving, allowing and settling a trustee's account and determining that income was currently distributable to the beneficiaries. (Citing *Freuler v. Helvering, supra.*)

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[10]In the *Henricksen* case notice was not given to all the interested parties. In this cause, respondent is faced with the fact that in addition to giving notice to the interested parties, respondent and all offices associated with respondent were given notice but failed to appear.

Moreover, in *Eisenmenger v. Commissioner of Internal Revenue,* 145 F. 2d 103 (8th Cir., 1944), the Court of Appeals held a state court decree, construing a trust, was binding upon the Commissioner although it was sought and rendered *after* the same issue had been decided against the taxpayer by the Board of Tax Appeals. Of course, the Commissioner in the *Eisenmenger* case raised the cry of "collusion."[11]

Also see:

Channing v. Hassett, 200 F. 2d 514 (1st Cir., 1952);

Nashville Trust Co. v. Commissioner of Internal Revenue, 136 F. 2d 148 (6th Cir., 1943);

Estate of Beachy, 15 T. C. 136 (1950).

As in the *Goodwin* case, the parties having adverse interests were before the Court. It was incumbent upon Miss Shortall, as guardian, to take prompt steps to protect the property of the minor upon learning for the first time that some one considered the 1943 gift by petitioner as being a revocable gift, particularly in view of the fact that petitioner had been dissipating her own assets and might cast covetous glances at the $317,360.59 held by the guardian for the minor. [R. 21, 83-88, 172-174.]

We submit that the validity of the Probate Court proceedings should be presumed. That such presumption is not overcome because there was not a "hotly contested" or "bitter court battle."

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[11]We respectfully submit that that cry of "collusion" is in effect an attack upon the integrity of our state courts. The Commissioner seems to take the position that unless proven otherwise, we are to assume that Probate Courts act *"pro forma"* and will sign anything the attorneys appearing before them may request.

We further submit that the California Probate Court is a court of a sovereign state and it is an integral and respected part of the judicial branch of the California government. Its integrity is presumed; we are not to presume that the Judges of that Court "rubber stamp" what is put before them by the attorneys. Accordingly, the integrity of the Probate Court Order [R. 83-88] is to be presumed and is binding upon respondent.

The Tax Court, in rejecting the California decree on the basis that there was no controversy between the parties cites the *Estate of Ralph Rainger,* 12 T. C. 483 (1949), *affirmed,* 183 F. 2d 587 (9th Cir., 1950). However, the facts in the *Rainger* case are different than the facts presented herein.

The California Inheritance Tax Appraiser included in the Estate of Ralph Rainger, deceased, certain intangible property rights in connection with songs he had written during his lifetime. The executrix filed written objections to the inclusion of this property in Inheritance Tax Appraiser's report. While these proceedings were pending before the Probate Court, a federal estate tax controversy arose as to the inclusion of this property in decedent's estate, and as to whether the alleged property was held by decedent and the executrix as community property or as tenants in common. Thereupon, the executrix amended her objections to the Inheritance Tax Report to contend that if the Probate Court should find that the decedent owned the intangible property rights, that the rights were owned by decedent and the executrix as tenants in common and not as community property.

At the hearing on the objections in the Probate Court, the attorney for the State Controller openly stated in court that insofar as the State of California was con-

cerned, it was indifferent to the question of whether or not the property was held to be community property or tenancy in common. He stated that the issue did not make a "nickel's worth" of difference insofar as California inheritance tax was concerned. Accordingly, there were no adverse interests before the Probate Court. Under those facts, the Tax Court was justified in holding that there was no decision on the merits as to the community property issue.

The Tax Court decision herein also relied on *Saulsbury v. United States,* 199 F. 2d 578 (5th Cir., 1952). [R. 104.]

In the *Saulsbury* case the parties before the state court were a trustee and a beneficiary. The trustee wanted to borrow certain moneys and use the trust income to repay the loan. The beneficiary expressed no objection. The state court decreed that trust income could so be used. The state court did not decide whether the trust income was "distributable" to the beneficiary—which was the tax question presented to the Court of Appeals. The tax question was whether the income was taxable to the beneficiary pursuant to Section 162(b) of the Internal Revenue Code, *i. e.,* taxable as "distributable" income even though not distributed.

In ruling upon the taxation question, the Court of Appeals pointed out that the state "court did not determine whether the trustee or the beneficiary was entitled to the income therefrom." (*Id.,* 199 F. 2d at 581.) Therefore, the Court of Appeals did not have before it the problem of whether the state court decision was or was not binding upon the Commissioner.

Where adverse interests were before the Probate Court, where both parties were present in court and represented

by counsel, where the issue of revocability of the oral trust was squarely presented to the court, where there was no fraud or collusion, the best authority on the law of California is the Order of the California Probate Court. [R. 83-88.] And that decree stated that an oral irrevocable trust was created.

In the within action, we have the following elements to consider with respect to the California Probate Court decree:

1. Adverse interests were before the Court.
2. The Court had jurisdiction over the property.
3. The parties were present in Court and represented by counsel.
4. Evidence was taken by the Court.
5. Oral arguments were made to the Court.
6. The guardian would have been remiss in her fiduciary duties if she had not instituted the proceeding.
7. The Federal tax authorities were given notice of the proceeding.
8. The issue of revocability of the oral trust created in 1943 was squarely before the Court.
9. There was no fraud or collusion.

The Probate Court decree stated that an oral irrevocable trust was created in 1943, and we submit that this decree is the best evidence of the law of California applicable to the property in question and is binding on respondent.

II.

Petitioner Could Not Have Prevented the Distribution to the Guardian on May 2, 1946, or the Making of the Order Holding the Oral Trust Irrevocable.

While respondent and the Tax Court "brush away" the California Probate Court decree, the Tax Court Opinion does not state that petitioner stood the least possible chance of convincing the Probate Court in 1946 that the assets should not be distributed to the minor's guardian but should be returned to petitioner.

In this connection, the following facts should be considered:

1. Even if petitioner wanted to commit perjury and deny that she understood that she could never again touch the 800 shares of stock after she made an oral gift in her conversation with Mr. Goldman, she would find that her oral testimony would be controverted by Miss Shortall, an attorney-at-law. [R. 158-160.]

2. The written instrument prepared and signed by Mr. Goldman and agreed to by petitioner "individually" treated the 800 shares as a completed gift. [Ex. 2-B, R. 38-41.] The trustee agreed to hold the 800 shares for the minor daughter and such other property *as the minor daughter might thereafter deposit with him.* [R. 38.]

3. Petitioner indicated her acknowledgment of the completed gift when she signed said instrument on behalf of her daughter "as the mother and guardian" of her minor daughter. [R. 41.] This indicated that she recognized that the gift was complete and the agreement as to the terms and conditions under which Mr. Gold-

man held the 800 shares was between Mr. Goldman and the minor daughter.

4. If there was any ambiguity in the written instrument, her actions and the actions of Mr. Goldman would have clearly demonstrated the true intention of a completed oral gift in 1943. In light of her 1943 Gift Tax and 1943 to 1945 Income Tax Returns, petitioner was foreclosed from contending in the California Probate Court, in 1946 and in 1947, that she did not make a completed and irrevocable gift in 1943. [R. 27, 31-32, 35-37.]

While respondent contends (and the Tax Court held) that the completed gift was made on May 2, 1946, when the property was transferred to the minor's guardian, respondent does not directly contend that in May, 1946, petitioner could have convinced the Probate Court that the trust property should be returned to her and not delivered to the minor's duly appointed guardian. Accordingly, petitioner could not have done anything in July, 1947, to cause the Probate Court to reach a different result.

Nevertheless, the respondent takes the position that since petitioner did not "controvert" the position of the guardian, the Probate Court is to be ignored. However, no suggestion is made as to how the petitioner could successfully controvert the position of the guardian other than by perjury. Moreover, even if petitioner denied the oral conversations with Mr. Goldman, she could not overcome the written instrument [R. 38-41] wherein she acknowledged and agreed that her daughter was the owner of the 800 shares of Aztec Brewery Company stock.

III.

Petitioner Made a Completed Oral Gift in 1943.

There is uncontradicted evidence herein that early in January, 1943, petitioner, in the presence of Richard S. Goldman and Clarissa Shortall, created an oral irrevocable trust of 800 shares of stock in the Aztec Brewing Company, for the benefit of her daughter, Lois E. Senderman. This oral gift in trust was expressly made effective immediately and was expressly made irrevocable. [R. 125-128, 132, 158-160.] We submit that there is no basis for disregarding this uncontradicted and unimpeached testimony.

The oral gift in trust was not in any way contingent or conditioned upon the execution of the later written instrument. The written instrument was not executed at the time the oral trust was created but was prepared by Mr. Goldman some 6 or 7 months later. [R. 133, 160-162.] It is the common law rule, and the rule in California, that an irrevocable oral trust may be created, and upon such creation may be terminated or revoked only with the consent of all of the beneficiaries.

> *Hellman v. McWilliams,* 70 Cal. 449, 11 Pac. 659 (1886).

In *De Olazabal v. Mix,* 24 Cal. App. 2d 258, 260, 74 P. 2d 787, 788 (1937), the court held that it is "well settled that a trust in personal property need not be in writing, and that no set form of words is necessary to create a trust."

In Scott on Trusts (1939), Volume 3, Section 330.2, the author citing, among other authorities, *Taylor v. Bunnell,* 133 Cal. App. 177, 23 P. 2d 1062 (1933), states:

> "If the terms of the trust are not contained in a written instrument, the revocability of the trust depends upon the manifestation of the settlor's intention as determined by his words and conduct in the light of all the circumstances. Ordinarily, the inference is that the trust is irrevocable unless an intention to reserve a power of revocation can be gathered from the language used by the settlor or from the character of the trust or from the circumstances of its creation."

It is our position herein that the trust was expressly made irrevocable and nothing that was done subsequent thereto could make the completed gift an incomplete gift and make an irrevocable trust a revocable trust.

Respondent has placed great emphasis on California Civil Code, Section 2280. This code section was amended in 1931 to provide that, unless expressly made irrevocable by the instrument creating the trust, voluntary trusts are to be deemed revocable. Since an oral trust is not created by an instrument, we submit that Civil Code, Section 2280, has no applicability to the oral trust. However, we wish to emphasize that it is our basic contention that the oral trust was expressly made irrevocable, was intended to be irrevocable, and that at all times thereafter, petitioner and Mr. Goldman treated the gift of 800 shares as completed. If nothing further had been done; if no written instrument had been executed; if there had been no court proceedings; we submit that the oral gift made by petitioner in January, 1943, was complete and she could not revoke the oral trust which she then created and could not recover the 800 shares of stock she gave her daughter.

IV.

It Was Error for the Tax Court to Disregard the Oral Irrevocable Trust and Determine the Controversy on the Basis of the Written Instrument.

The written instrument involved was not labeled a declaration of trust; the instrument recited an acknowledgment by Mr. Goldman that he was holding, as trustee, certain shares of stock for petitioner and certain shares of stock for petitioner's minor daughter. It treated the transfer to the minor daughter of the beneficial interest of 800 of the shares already held by Mr. Goldman "as Trustee" as a *fait accompli.* In view of the fact that petitioner did not sign as trustor, but signed "individually" and "as mother and guardian" of the minor, plus the fact that "Trustee" agreed to hold other property *deposited with him by the minor* and agreed to deliver the property to the minor's duly appointed guardian, we submit that all the written instrument did was acknowledge that the oral completed gift had already been made.

The Tax Court Opinion states that its decision is based upon *Krag v. Commissioner of Internal Revenue,* 8 T. C. 1091 (1947), and *Gaylord v. Commissioner of Internal Revenue,* 153 F. 2d 408 (9th Cir., 1946), *affirming* 3 T. C. 281. We submit that the decisions in the *Krag* and *Gaylord* cases are distinguishable from the facts presented herein and inapplicable.

In the *Krag* case, the donor created a trust by written instrument in which the donor made himself trustee, and limited the period of time the trust was to remain in effect. The donor, by this written declaration of trust, reserved to himself broad powers as to control of the *res;* however, he did not reserve the right to change or revoke the trust.

In the *Krag* case the trust was created by the written instrument and that was the only act creating the trust. In the within cause, the trust was created orally and the written instrument was not the act that created the trust; the written instrument was a subsequent acknowledgment by Mr. Goldman that he held certain stock "as Trustee," that a portion of the stock was held for petitioner and a portion thereof for petitioner's minor daughter.[12]

The *Gaylord* case involved a written declaration of trust executed in 1935 whereby the donors declared themselves trustees. In the *Gaylord* case, this Court pointed out that the grantors retained powers of management and control over the trust corpus as though they were the absolute owners; their discretion was absolute and uncontrolled and its exercise conclusive on all persons; the donors were able to continue to deal with the property which was the subject of the gift as absolute owners thereof. (*Gaylord v. Commissioner of Internal Revnue, supra,* 153 F. 2d at p. 412.) These facts are unlike the facts herein, where the donor orally made a completed gift in trust, retained no powers over the property, and the written instrument prepared 6 or 7 months later by the trustee (and agreed to by the donor) acknowledged that the minor daughter "owned" the beneficial interest in the 800 shares of stock and did not recite that the donor was giving that to her

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[12]We submit that it should be kept in mind that at the time petitioner created the oral trust in January of 1943, the certificates of stock in question were already in the name of Richard S. Goldman, "as Trustee." [R. 129.]

daughter—the instrument said the daughter "owned" the stock.

The Tax Court in this cause held:

> "* * * On the authority of the *Krag* and *Gaylord* cases cited above, we sustain respondent's holding that the 1943 written trust, here under study, was a revocable trust; that whatever its form, the oral trust was superseded by the written trust; that the transfer of title occurred in 1946 when the written trust was terminated and the trust property transferred to the guardian for the minor, and that petitioner should be taxed accordingly." [R. 107.]

There are three separate holdings in the above quoted portion of the Tax Court Opinion which we would like to consider.

The Tax Court holds that the written instrument was "a revocable trust." The next portion of this Argument will consider that holding in detail. In any event, the written instrument itself is the best evidence and the most persuasive argument against this contention. The written instrument clearly and expressly treats the gift to the minor daughter as completed and irrevocable.

The Tax Court next holds that the oral trust was superseded by the written trust. In this connection, it should be noted that the written instrument in question was not a formal declaration of trust by petitioner; it didn't purport to do anything more than acknowledge that Mr. Goldman had some stock in his name that he was holding for petitioner and for her daughter.

The written instrument treated the gift of the 800 shares of stock as completed. Moreover, Mr. Goldman had no right, whether by mistake or by reason of a document not precisely drawn, to change the legal effect of a complete transaction.[13]

The Tax Court then goes on to hold that the transfer of title occurred in 1946 when the trust was terminated and the trust property transferred to the guardian for the minor. We submit that, subsequent to 1943, there was nothing petitioner could have done to prevent the distribution to the minor's guardian. In this connection, we wish to again stress that the written instrument treated the beneficial interest of the 800 shares as belonging to the minor; and Mr. Goldman entered into an agreement with the minor, through petitioner as her mother and natural guardian, that if a duly appointed guardian of the minor was ever appointed, he would deliver that property, and any other property the minor might deposit with him, to such guardian.

Regardless of the death of Mr. Goldman, the assets held by him on behalf of the minor would have been distributed to the duly appointed guardian of the minor whenever such guardian was appointed.

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[13]In the *Krag* and *Gaylord* cases the written instruments were prepared and executed at the time the transaction was consummated and were the means whereby the trust was created. In the within cause, the written instrument was executed 6 or 7 months later and did not, by its terms, purport to be the instrument making the gift.

V.

The Written Instrument Did Not Create a Revocable Trust.

It is the basic contention of petitioner that there was a completed oral gift in 1943. However, the Tax Court has taken the position that since there was a subsequent written instrument, the evidence of an earlier oral irrevocable trust is to be ignored.

The Tax Court relied upon California Civil Code, Section 2280, which provides, in part, as follows:

> "Unless expressly made irrevocable by the instrument creating the trust, every voluntary trust shall be revocable by the trustor by writing filed with the trustee. * * *."

In its Opinion, the Tax Court said:

> "* * * We find it impossible to believe that Goldman, an experienced lawyer, presumptively familiar with the provisions of Section 2280 of the California Code and cognizant of all the facts, would inadvertently omit from the declaration of the trust the express provision called for by the statute. One sentence of five words would have sufficed to have removed all questions as to the revocability of the trust. * * *." [R. 107.]

If Mr. Goldman were alive, he would be in the position to answer the Tax Court. While giving due deference to the fact that we are discussing the work of a deceased attorney, we shall attempt to explain what the Tax Court found so difficult to believe.

We would like to first note that when Mr. Goldman went to law school and during his first two decades of

practice in San Francisco, it was the common law rule and the rule in California that a trust could not be revoked unless the power of revocation was expressly reserved.

Prior to 1931, California Civil Code, Section 2280, read as follows:

> "A trust cannot be revoked by the trustor after its acceptance, actual or presumed, by the trustee and beneficiaries, except by the consent of all the beneficiaries, unless the declaration of trust reserves a power of revocation to the trustor, and in that case the power must be strictly pursued."

With this 1931 change in the common law in mind, we submit that the Tax Court was unfair to petitioner in making the presumption that if an irrevocable trust was intended, Mr. Goldman could not have possibly failed to use the words: "This trust is irrevocable."

Moreover, and in fairness to Mr. Goldman, we submit that the written instrument which he signed made it clear that petitioner reserved no control whatsoever over the 800 shares held by Mr. Goldman for the minor daughter. It was not an instrument framed as a declaration of trust by petitioner; accordingly, Mr. Goldman saw no necessity of discussing revocability or irrevocability as he treated the gift as completed and stated that the 800 shares of stock were owned by the minor.

We respectfully submit that the answer to the controversy presented herein can be found by a close scrutiny of the written instrument. [R. 38-41.]

The written instrument signed by Mr. Goldman stated:

1. I have in my possession 2396⅞ths shares of Aztec Brewery Company stock, which shares stand in my name as "Trustee." [R. 38.][14]

2. Lois J. Senderman (the petitioner herein) is the beneficial owner of 1596⅞ths of said shares of stock. [R. 38.]

3. Lois E. Senderman, a minor, is the owner of 800 shares. [R. 38.]

4. I agree to hold the minor's 800 shares "and any other property" *the minor* "may hereafter deposit with" me upon the terms and conditions set forth. [R. 38.]

5. I agree to collect the income on the minor's property and to reinvest it. I'll pay the expenses and pay myself a reasonable fee. [R. 38.]

6. I shall have *"the sole and uncontrolled discretion"* to give the minor such income and principal as is in her best interests. [R. 38-39.]

7. If a guardian is ever duly appointed for the minor, I'll turn the property over to the minor's guardian.

8. If no such guardian is ever appointed, I'll give the minor her property when she is 21. [R. 39.]

9. If the minor dies, I'll give her property to her personal representative. [R. 39.]

10. If I don't want to hold the minor's property, I can take action to turn it over to her duly appointed guardian. [R. 39.]

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[14]Two shares were in Mr. Goldman's possession but were not in his name as "Trustee."

11. If I die, then my executors can take the necessary action to turn the minor's property over to her duly appointed guardian. [R. 39-40.]

12. I will render annual accountings. [R. 40.]

13. I am not responsible for any losses or errors in judgment, unless I am wilfully negligent. [R. 40.]

14. Upon termination of my liability as Trustee, I will reimburse myself for all expenses and charges. I can also hold back enough money to take care of contingent obligations. [R. 40.]

15. After payment of all these obligations, I will turn the minor's property over to her. [R. 40.]

16. I want Lois J. Senderman to agree to this "individually" because I want her to be bound to the recital that her minor daughter, Lois E. Senderman, is the "owner of 800 shares" of the Aztec Brewery Company stock. [R. 38, 41.]

17. Since I am entering into an agreement with the minor daughter, Lois E. Senderman, as to the terms and conditions under which I will hold her property (the 800 shares of stock and any other property the minor may deposit with me), and since she has no duly appointed guardian, I want her mother, as the minor's natural guardian, *to agree on behalf of the minor* as to such terms and conditions. [R. 38, 41.]

With this paraphrase of the written instrument, we submit is abundantly clear that Mr. Goldman was saying that, as to the 800 shares, that stock belongs to the minor, Lois E. Senderman, and Lois J. Senderman (petitioner) has no interest therein.

In plain language Mr. Goldman said the minor owns 800 shares and her mother can't get it back.

The Tax Court, citing California Civil Code, Section 2280, held that Mr. Goldman's failure to use the word "irrevocable" in the written instrument is controlling. We submit that when the true nature of the instrument is considered, it becomes clear that Section 2280 is not applicable to such an instrument.

Moreover, Section 2280 uses the phrase "unless expressly made irrevocable" but there is no requirement that the trust instrument use the word "irrevocable." We submit that even without using that magic word, Mr. Goldman's written instrument made it clear that petitioner couldn't get the 800 shares back.

Under the common law rule requiring express reservation of the power of revocation, it was not necessary to reserve the power in *haec verba,* but reservation of the power could "be indicated by the use of language from which it may be inferred." (*Scott on Trusts,* Vol. 3, Sec. 330.1, p. 1797.)

California Civil Code, Section 2280, as originally enacted in 1872, was in effect an adoption of the common law rule that power to revoke had to be reserved. In 1931, this Code section was amended to reverse the rule to overcome the harshness attendant upon inadvertent failure to include a power of revocation. (Cal. Stats. 1931, p. 1955.) The present version was designed to shield settlors against technical errors in draftsmanship. (See *Comment,* 28 Cal. L. Rev. 202, 208 [1940].) The 1931 revision was a remedial statute enacted for the benefit of settlors.

The respondent now seeks, by asking for a strict and narrow construction of the statute, to turn the statute against the settlor who is supposed to be protected by the

statute. We submit that in a case like this where it is conceded that the intent of the settlor was to create an irrevocable trust, where the acts of the settlor precedent to and subsequent to the trust support the contention of irrevocability, the burden should be placed upon respondent to show that such was not the case.

California Civil Code, Section 4, provides:

> "The rule of the common law, that statutes in derogation thereof are to be strictly construed, has no application to this code. The code establishes the law of this state respecting the subjects to which it relates, *and its provisions are to be liberally construed with a view to effect its objects and to promote justice."* (Emphasis supplied.)

Decisions with respect to the imposition of taxes should be based on "rational foundations" and not on "linguistic refinement" or the "niceties of the art of conveyancing." (See *Helvering v. Hallock,* 309 U. S. 106, 117, 60 S. Ct. 444, 450 (1940).)

The realities of the taxpayer's economic interest rather than the niceties of the conveyancer's art should determine the power of tax.

> *Helvering v. Safe Deposit & Trust Co. of Baltimore,* 316 U. S. 56, 58, 62 S. Ct. 925, 927 (1942);
>
> *Curry v. McCanless,* 307 U. S. 357, 59 S. Ct. 900 (1939).

> "The rule that the substance of a transaction rather than its mere form, controls tax liability, is one of very wide application. * * * Numerous decisions of the Supreme Court and hundreds of decisions of lower courts have discussed and applied the rule and it is also incorporated in several sections of the (In-

ternal Revenue) Code and the (Treasury) Regulations." (3 *Prentice-Hall Federal Tax Service* (1954), ¶28, 201.)

The Prentice-Hall Tax Service, in its discussion of this basic general principle of the tax law, points out that questions of "substance v. form" are usually raised by the Government, but occasionally the Government is on the other side of the argument. We submit that in the within controversy, the respondent recognizes that as a matter of substance the petitioner gave her daughter 800 shares of Aztec Brewery Company stock in 1943, but seeks to impose $300,000.00 of tax on this $30,000.00 gift because of the form of the transaction.

Moreover, the language in the written instrument clearly and unambiguously provides that insofar as petitioner is concerned, she has already made a completed gift of 800 shares of Aztec Brewery Company stock to her minor daughter and her minor daughter is the absolute and unqualified owner of the beneficial interest in said stock.

Even if the language be considered uncertain or ambiguous, the instrument is to be construed in favor of the beneficiary. (*Ball v. Mann,* 88 Cal. App. 2d 695, 199 P. 2d 706 (1948).)

As heretofore noted, the construction placed on the instrument by the acts of the parties, by filing gift tax returns and otherwise, requires that the ambiguity, if any, be construed to mean that an irrevocable completed gift was made in 1943.[15]

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[15]To borrow a phrase from the Tax Court Opinion—"actions speak louder than words." [R. 106.]

VI.

The Transfer of the Assets to the Guardian in 1946 Did Not Constitute a Taxable Gift.

Assuming, for the sake of argument only, that the irrevocable transfer of the property occurred on May 2, 1946 (the day the Probate Court transferred the assets to the guardian), then even in that event there was no taxable gift in 1946 under the doctrine of *Harris v. Commissioner of Internal Revenue,* 340 U. S. 106, 71 S. Ct. 181 (1950). Under the rule of the *Harris* case, transfers pursuant to court order are not subject to gift tax, regardless of the adequacy of the consideration.

In the *Harris* case, the Supreme Court considered a property settlement agreement between husband and wife which, by its terms, became operative when either party obtained a divorce. The agreement further provided that the agreement should be submitted to the divorce court "for its approval."

When the taxpayer divorced her husband in 1943, the property settlement agreement was incorporated in the divorce decree. It was found that the value of the property transferred to the taxpayer's husband exceeded that received by petitioner by $107,150.00. The Commissioner assessed a gift tax on the theory that any rights which the husband might have given up by entering into the agreement could not be adequate and full consideration. (*Id.,* 340 U. S. at p. 109, 71 S. Ct. at p. 183.)

The Supreme Court agreed that, based on the agreement alone, "there would be no question that the gift tax would be payable." (*Id.,* 340 U. S. at p. 109, 71 S. Ct. at p. 183.)

However, the Supreme Court held that the transfer was not made pursuant to a promise or agreement but was made pursuant to the state court decree and therefore not subject to gift tax although the decree was based upon the written agreement.

> "* * * It is 'the transfer' of the property with which the gift tax statute is concerned, not the sanctions which the law supplies to enforce transfers. If 'the transfer' of marital rights in property is effected by the parties, it is pursuant to a 'promise or agreement' in the meaning of the statute. If 'the transfer' is effected by court decree, no 'promise or agreement' of the parties is the operative fact. In no realistic sense is a court decree a 'promise or agreement' between the parties to a litigation. If finer, more legalistic lines are to be drawn, Congress must do it." (*Id.*, 340 U. S. at pp. 111-112, 71 S. Ct. at p. 184.)

While the *Harris* case involved a property settlement agreement incident to a divorce, the doctrine of that case is not limited to such a situation; it is applicable in all cases where a transfer of property is made pursuant to a state court order, even though the state court order is based on a prior agreement of the parties. There is nothing in the gift tax law that would justify limiting the rule to divorce settlements.

In 1946 the property here in question was transferred pursuant to the Order of the Probate Court; the Order recited the provisions of the written instrument as to appointment of a guardian of the minor and transfer of the property to the guardian. [R. 65-72.] Under the *Harris* rule, transfers pursuant to court order are not subject to a gift tax, regardless of the adequacy of the consideration.

The Tax Court held that the *Harris* case was not applicable herein because in the *Harris* case the element of donative intent was absent. We submit that the only donative intent of petitioner was in 1943, when she created the oral irrevocable trust. The subsequent written instrument was simply an acknowledgment that the gift had been made; and that it was executed in 1943. Accordingly, a holding that there was intent to make a completed gift in 1946 and not in 1943 strains every sense of justice and equity.

Petitioner's contention is that the completed gift was made in 1943. Respondent contends (and the Tax Court held) that the gift was made on May 2, 1946, when the Probate Court made an Order transferring the property to the guardian.[16] If that be respondent's contentention, then respondent is faced with the fact that he has brought the controversy within the rule of the *Harris* case.

In the *Harris* case, the Supreme Court noted that "the purpose of the gift tax is to complement the estate tax by preventing tax-free depletion of the transferor's estate during his lifetime." (*Id.,* 340 U. S. at p. 107, 71 S. Ct. at p. 182.]

We submit that in the within cause the respondent is seeking to enforce the gift tax so that the petitioner's estate will be completely depleted during her lifetime by the payment of $300,000.00 in tax on a $30,000.00 gift.

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[16]Petitioner's position is that in 1946 the Probate Court simply transferred the *minor's property* from the Trustee to the duly appointed guardian for the minor.

Conclusion.

The uncontradicted evidence establishes that in 1943, petitioner made a completed gift to her minor daughter of 800 shares of Aztec Brewing Company stock. This was done by petitioner's oral directions to Richard S. Goldman, in the presence of Clarissa Shortall.

The subsequent written instrument prepared and executed by Mr. Goldman expressly and explicitly stated that the 800 shares were "owned" by petitioner's minor daughter.

The right of the minor to have her property (the 800 shares and other property the minor might deposit with Mr. Goldman) held by Mr. Goldman delivered to her duly appointed guardian was set forth in said written instrument. Accordingly, the Order of the Probate Court on May 2, 1946, transferring the minor's property to her guardian was an act the petitioner could not have prevented.

Aside from the rule of the *Harris* case, we submit there is nothing in the record to justify a finding that the petitioner made a completed gift on May 2, 1946, by reason of said Probate Court Order.

Moreover, the law of California determines when the completed gift was made and the Order of the California Probate Court is the best authority on that subject. The California Probate Court held that an oral irrevocable trust was created by petitioner in 1943. The Tax Court erred in not following that Order.

We respectfully submit petitioner made a completed gift in 1943 and not in 1946, and, accordingly, there is no deficiency in gift tax for the year 1946.

Respectfully submitted,

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